Lai Kok Kit @ Sulaiman Lai bin Abdullah v MBf Finance Bhd

COURT OF APPEAL (KUALA LUMPUR) — CIVIL APPEAL NO B-02-227 OF 1996
GOPAL SRI RAM, HAIDAR JJCA AND AZMEL J
3 APRIL 2000

Contract *— Breach — Contract to restructure loan — Defendant fail to cancel order for sale in accordance with contract — Whether plaintiff can later refuse to continue performance of his obligations in view of defendant's default*

Contract *— Frustration — No fundamental or radical change in circumstances — Test to be applied — Contract to restructure loan — Defendant fail to cancel order for sale in accordance with contract — Whether amount to frustration — Contracts Act 1950 s 57(2)*

The plaintiff was the registered proprietor of a double storey terrace house in Klang ('the subject property'). In 1987, the plaintiff charged the subject property to the defendant to secure a loan of RM80,000 which was made under an agreement dated 28 August 1987 ('the first agreement'). The plaintiff defaulted in making repayment and the defendant instituted foreclosure proceedings for the sale of the subject property by way of public auction. Later, an agreement was entered into between the plaintiff and the defendant to restructure the loan facility that formed the subject matter of the first agreement. On 14 June 1989, the defendant wrote to the plaintiff a letter setting out the terms and conditions of the restructure which the plaintiff had accepted ('the second agreement'). The defendant granted the plaintiff a fresh loan of RM80,000 and a personal loan of RM5,000. The obligation on the defendant under the second agreement was to cancel or withdraw the order for sale. On 27 July 1989, the defendant wrote to the land administrator. It asked for the auction to be adjourned until November 1989. But it did not ask for cancellation or withdrawal of the sale. The land administrator refused the adjournment. Subsequently, the defendant applied to the High Court for an order setting aside the order for sale made by the land administrator. On 8 April 1991, the High Court declined the defendant's application. From about June 1991 onwards, the plaintiff ceased to honour his part of the bargain.

The defendant then took out two actions against the plaintiff. The action in the magistrates' court was for the recovery of the balance due under the personal loan granted under the second agreement while the action in the sessions court was to recover the whole of the balance due under the first agreement. The plaintiff also took out proceedings against the defendant for negligence and for breach of contract which were tried by the High Court. The learned judge found that the main object of the second agreement had been rendered impossible of performance. Counsel for the plaintiff argued that the learned judge was wrong in treating this case as one coming

within the doctrine of frustration. His argument is that this is a case of an obligation voluntarily undertaken by the defendant, namely to withdraw or cancel the order for sale. And the defendant had plainly failed to fulfill that obligation and once the second agreement had taken effect, the first agreement was at an end. However counsel for the defendant argued that the express clause contained in the second agreement entitles the defendant to revert to the original position whenever there is a default. Counsel has drawn the court's attention to the fact that the plaintiff had defaulted in his obligation since June 1991.

Held, allowing the appeal:

(1) After a contract has been entered and there is a change of circumstances which do not render a fundamental or radical change in the obligation originally undertaken to make the performance of the contract something radically different from that originally undertaken, the contract does not become impossible and it is not discharged by frustration (see p 143F); *Ramli bin Zakaria & Ors v Government of Malaysia* [1982] 2 MLJ 257 followed. The present case concerns a change in circumstances that were not radically different from those that prevailed at the time the second agreement was entered into. All that had happened was that the defendant had failed to pursue its best endeavours to secure the sale or withdraw the order for sale (see p 144B–C).

(2) The primary obligation under the second agreement was on the defendant to do what it promised, namely to have the order for sale cancelled or withdrawn. By June 1991 (date of the alleged default by the plaintiff), that obligation remained plainly unfulfilled. Since the defendant had breached its part of the bargain, it does not lie on its mouth to complain of the plaintiff's default. The plaintiff was clearly within his rights to refuse to continue performance of his obligations under the contract in view of the defendant's default (see pp 144I–145A).

(3) Upon the making of the second agreement and upon the defendant's breach of it, the rights of the parties were to be determined in accordance with that agreement. The defendant did not have the right to have recourse to the first agreement. Accordingly, the sums claimed by it in the sessions court action were clearly irrecoverable. However, the plaintiff was under a separate obligation to pay and settle the personal loan given him under the second agreement (see p 145B–C).

[Bahasa Malaysia summary

Plaintif adalah tuan punya berdaftar suatu rumah teres dua tingkat di Klang ('hartanah tersebut'). Pada tahun 1987, plaintif telah

menggadaikan hartanah tersebut kepada defendan untuk menjamin suatu pinjaman sebanyak RM80,000 yang dibuat di bawah perjanjian bertarikh 28 Ogos 1987 ('perjanjian pertama tersebut'). Plaintif telah ingkar di dalam membuat pembayaran balik dan defendan telah memulakan prosiding penutupan untuk menjual subjek hartanah tersebut melalui lelong awam. Kemudian, suatu perjanjian telah dimasuki antara plaintif dan defendan untuk menyusun semula kemudahan pinjaman yang membentuk perkara subjek perjanjian pertama. Pada 14 Jun 1989, defendan telah menulis kepada plaintif suatu surat membentangkan terma-terma dan syarat-syarat penyusunan semula tersebut di mana plaintif telah menerima ('perjanjian kedua tersebut'). Defendan telah memberikan plaintif suatu pinjaman baru sebanyak RM80,000 dan pinjaman peribadi sebanyak RM5,000. Kewajipan di atas defendan di bawah perjanjian yang kedua adalah untuk membatalkan atau menarik balik perintah jualan. Pada 27 Julai 1989, defendan telah menulis kepada pentadbir tanah. Ia meminta agar lelongan tersebut ditangguh sehingga November 1989 tetapi ia tidak meminta pembatalan atau penarikbalikan penjualan tersebut. Pentadbir tanah enggan memberikan penangguhan tersebut. Kemudian defendan memohon kepada Mahkamah Tinggi untuk perintah mengetepikan perintah jualan yang dibuat oleh pentadbir tanah. Pada 8 April 1991, Mahkamah Tinggi tidak membenarkan permohonan defendan. Mulai lebih kurang bulan Jun 1991, plaintif tidak menunaikan kewajipannya di bawah perjanjian tersebut.

Kemudian defendan mengeluarkan dua tindakan terhadap plaintif. Tindakan di mahkamah majistret adalah untuk mendapatkan kembali baki yang masih tertunggak di bawah pinjaman peribadi yang diberikan di bawah perjanjian kedua sementara tindakan di mahkamah sesyen adalah untuk mendapat kembali semua baki yang tertunggak di bawah perjanjian pertama. Plaintif juga membawa dua tindakan terhadap defendan untuk kecuaian dan untuk pelanggaran kontrak yang dibicarakan oleh Mahkamah Tinggi. Hakim yang arif mendapati bahawa objek utama perjanjian yang kedua telah menjadi mustahil untuk dilaksanakan. Peguam plaintif menghujahkan bahawa hakim yang arif telah silap kerana menganggap kes ini sebagai sesuatu yang diliputi oleh doktrin kekecewaan. Hujahannya adalah bahawa ini adalah suatu kes di mana suatu kewajipan telah diakujanjikan dengan sukarela oleh defendan, iaitu untuk menarik balik atau membatalkan perintah jualan tersebut, dan defendan telah gagal untuk menunaikan kewajipan tersebut dan sebaik saja perjanjian kedua mula berkuatkuasa, perjanjian pertama telah tamat. Namun peguam untuk defendan telah berhujah bahawa fasal nyata yang terkandung di dalam perjanjian yang kedua memberikan hak kepada defendan untuk berbalik semula kepada kedudukan asal apabila terdapat keingkaran. Peguam telah membawa perhatian mahkamah kepada fakta bahawa plantif telah ingkar di dalam kewajipannya sejak Jun 1991.

Diputuskan, membenarkan rayuan tersebut:

(1) Selepas suatu kontrak dimasuki dan terdapat perubahan keadaan-keadaan yang bukanlah suatu perubahan yang besar atau radikal di dalam kewajipan yang diakujanji pada asal untuk menjadikan pelaksanaan kontrak sesuatu berbeza secara radikal daripada apa yang diakujanji pada asalnya, kontrak tersebut tidak menjadi mustahil dan tidak dilepaskan melalui kekecewaan (lihat ms 143F); *Ramli bin Zakaria & Ors v Government of Malaysia* [1982] 2 MLJ 257 diikut. Kes ini adalah berkaitan dengan perubahan keadaan-keadaan yang bukanlah berbeza secara radikal daripada apa yang berlaku pada masa perjanjian kedua dimasuki. Apa yang berlaku hanyalah defendan gagal untuk menjalankan usaha terbaiknya untuk menjamin jualan tersebut dan untuk menarik balik perintah jualan tersebut (lihat ms 144B–C).

(2) Kewajipan asal di bawah perjanjian yang kedua adalah di atas defendan untuk membuat apa yang ia telah janjikan, iaitu untuk membatalkan atau menarikbalik perintah jualan tersebut. Menjelang Jun 1991 (tarikh keingkaran oleh plaintif yang dikatakan), kewajipan tersebut kekal tidak dapat dipuaskan. Oleh kerana defendan telah ingkar dalam kewajipannya, ia tidak boleh mengadu akan keingkaran plaintif. Plaintif dengan jelas berhak untuk enggan meneruskan pelaksanaan kewajipannya di bawah kontrak memandangkan keingkaran defendan (lihat ms 144I–45A).

(3) Selepas membuat perjanjian yang kedua dan selepas keingkaran defendan, hak-hak pihak-pihak adalah ditentukan menurut perjanjian tersebut. Defendan tiada hak untuk menggunakan perjanjian pertama. Dengan itu, jumlah tersebut yang dituntut olehnya di dalam tindakan mahkamah sesyen adalah jelas tidak boleh didapat kembali. Namun, plaintif adalah di bawah kewajipan yang berbeza untuk membayar dan menyelesaikan pinjaman peribadi yang telah diberikan kepadanya di bawah perjanjian kedua tersebut (lihat ms 145B–C).]

Notes

For cases on breach generally, see 3 *Mallal's Digest* (4th Ed, 1997 Reissue) paras 1611–1693.

For cases on frustration generally, see 3 *Mallal's Digest* (4th Ed, 1997 Reissue) paras 2216–2239.

Cases referred to

Dalmia Dairy Industries Ltd v National Bank of Pakistan [1978] 2 Lloyd's Rep 223 (refd)

Dato Yap Peng v Public Bank Bhd [1997] 3 MLJ 484 (refd)

Ramli bin Zakaria & Ors v Government of Malaysia [1982] 2 MLJ 257 (folld)

Supamarl Ltd v Federated Homes Ltd (1981) 9 Con LR 25 (refd)

Legislation referred to

Civil Law Act 1956 s 15
Contracts Act 1950 s 57(2)
National Land Code 1965 ss 263, 265, 418

SS Ravichandran (*V Meena* with him) (*Seah Balan Ravi & Co*) for the appellant.

Paramjit Kaur (*HY Loo & SP Ng* with her) (*JM Chong, Vincent Chee & Co*) for the respondent.

Gopal Sri Ram JCA (delivering the oral judgment of the court): This appeal has been brought against the decision of the High Court at Shah Alam which found for the respondent on the point of frustration. It is necessary to hearken to the facts of this case in order to appreciate the issues that the appeal raises.

For convenience, we will refer to the parties according to the titles assigned to them in the court below.

The plaintiff was the registered proprietor of a double-storeyed terrace house in Klang ('the subject property'). In 1987 the plaintiff charged the subject property to the defendant to secure a loan of RM 80,000. The loan was guaranteed by two persons who are not concerned in this appeal. At some point after the disbursement of the loan, the plaintiff defaulted in making repayment. For completeness we will say that that loan was made under agreement dated 28 August 1987 ('the first agreement'). Following the plaintiff's default, the defendant instituted foreclosure proceedings for the sale of the subject property by way of public auction. Those proceedings were instituted before the Land Administrator Klang who, on 17 December 1988, granted an order for sale pursuant to s 263 of the National Land Code 1965.

The first public auction for the sale of the subject property was fixed on 21 March 1989. But there were no bidders. So the auction was aborted. There then followed a train of events that has led to the present litigation.

In or about June 1989, the plaintiff approached the manager of defendant's branch in Klang (DW1 in the court below). The learned judge found; and we accept his finding on this point; that an agreement was entered into between the plaintiff and the defendant to restructure the loan facility that formed the subject matter of the first agreement.

On 14 June 1989, the defendant wrote to the plaintiff a letter setting out the terms and conditions of the restructure. It is an important document and has a significant bearing upon this case. For that reason we will reproduce the main parts of that letter. This is what it says.

> We refer to the above and are pleased to inform you that your request to restructure the above loan has been approved in principle. As such, the amended terms and condition are as follows:
>
> (i) Restructured amount — RM80,000.
>
> (ii) Period — 19 years (228 months) inclusive of 36 months grace period for monthly interest servicing.

(iii) Interest rate — 8.50% pa AR (remain unchanged).

(iv) Repayment — Interest to be serviced monthly for 36 equal months; the first month to be due and payable on 1 July 1989 and thereafter by 192 equal monthly installment of principal and interest of RM777,42 each.

Please take note that you are required to give us an irrevocable undertaking letter from your employer, KCT to deduct your salary as follows and the cheque made payable in favour of MBf Finance Bhd:

(i) Personal Loan Repayment – PLPK 414 — RM716.40

(ii) Housing Loan Repayment – HLPK 249 — RM566.67

Total Deduction RM743.07

and the first deduction must reach us on or before the first (1st) of every month wef 1 July 1989.

In the event of default of the above terms and condition, we reserve the right to revert back to the present status. This restructuring plan would then deem to be revoked and thereafter legal proceedings will be continued without further reference to you.

Kindly signify your acceptance to the above by signing and returning to us the duplicate copy of this letter within 14 days from date hereof together a sum of RM608 being the differential sum between your outstanding balance and the restructured amount failing which the above approval is deemed cancelled.

If you have further queries, please do not hesitate to contact the undersigned. (Emphasis added.)

The plaintiff accepted the terms set out in the aforesaid letter by signing a copy of it. We will refer to this document as 'the second agreement'.

Following the execution of the second agreement, steps were taken to implement its terms. This was done by the defendant granting the plaintiff a fresh loan of RM80,000 and a personal loan of RM5,000. The latter sum was to be utilized to settle the arrears of interest due under the first agreement. The plaintiff opened a savings account with the defendant into which he paid his salary. The defendant debited the instalments payable under the second agreement from that account.

The obligation on the defendant under the second agreement was, as found by the judge, to cancel or withdraw the order for sale. The defendant did in fact take some steps in this direction.

On 27 July 1989, it wrote to the land administrator. It asked for the auction to be adjourned until November 1989. But it did not ask for cancellation or withdrawal of the sale. The land administrator refused the adjournment.

Subsequently, the defendant applied to the High Court in Shah Alam. Its application is dated 3 April 1991. It moved the court for an order setting aside the order for sale made by the land administrator. On April 8 1991, the High Court declined the defendant's application.

From about June 1991 onwards, the plaintiff ceased to honour his part of the bargain. The defendant then took out two actions against the plaintiff. One action was in the magistrates court. It was for the recovery of

the balance due under the personal loan granted under the second agreement. The other action was commenced in the sessions court. It was to recover the whole of the balance due from the plaintiff to the defendant under the first agreement. A

We may mention that in the meantime the subject property had been sold by public auction. But the sum realized was insufficient to satisfy the defendant's claim under the first agreement. The shortfall was about RM22,000. The sessions court's action sought to recover that sum. B

In the meantime, the plaintiff also took out proceedings. He sued the defendant for negligence and for breach of contract. The essence of his complaint was that the defendant had breached its obligation to obtain a withdrawal or cancellation of the order for sale. C

All three actions were tried by the High Court in Shah Alam. The learned judge found, as we have already said, that there was an agreement between the parties under which the defendant had undertaken an obligation to cancel or withdraw the land administrator's order for sale. However, the learned judge went further. He found that the main object of the second agreement had been rendered impossible of performance. He held that it was frustrated. He then purported to act under s 15 of the Civil Law Act 1956 to adjust the rights of the parties. The learned judge however negatived negligence on the part of defendant. D

Before us, Mr Ravichandran of counsel for the plaintiff has not sought to question the finding of the learned judge on the issue of negligence. He has however criticized the learned judge's finding upon the issue of frustration. And it is to that point that we must now address our minds. E

The essence of Mr Ravichandran's complaint is that the learned judge was wrong in treating this case as one coming within the doctrine of frustration. He says that the learned judge ought to have dealt with the case purely on the footing of a breach of contract. His argument is that this is a case of an obligation voluntarily undertaken by the defendant, namely to withdraw or cancel the order for sale. And the defendant had plainly failed to fulfil that obligation. F

Counsel further argues that once the second agreement had taken effect, the first agreement was at an end, so that a breach of the former does not revive the latter. In support of this argument he read to us a passage from the decision in *Supamarl Ltd v Federated Homes Ltd* (1981) 9 Con LR 25, at p 34 which is as follows: G

> In any event, in my view, a failure by Federated to honour such a term, even if it were part of a compromise agreement, would not entitle Supamarl to treat the compromise agreement as repudiated, and in fact they have never sought to do so until after the relationship between the parties had come to an end in October 1976. Having regard to my finding that Federated lawfully terminated the contract, Mr Blackburn's second line of argument does not arise. However, in case it is of any assistance, I shall state my views on it. I accept Mr Smith's suggestion that in the present case we are dealing with a promise for a promise type of accord and satisfaction and not one which depended upon the actual performance of that which had been promised by H I

Federated. It is to be noted in favour of Federated that the first two instalments of £5000 each were paid as and when due.

> In such circumstances, in my judgment, the original claims ceased to exist and *the liability thereunder was discharged when the compromise agreement was entered into and these original claims cannot be revived whatever may have happened to that agreement* and whether or not it has been repudiated, either because a breach of the agreement as such or if in fact there was a repudiation arising out of the repudiation of the main contracts had *Supamarl*'s case on the first issue been correct. I do not think that the claims made in March 1976 can be revived in any form whatsoever, either on the basis of quantum meruit or on any other basis. I think that *once the original claims were compromised effectively in a binding agreement, the only remedy that Supamarl would have would be to claim for damages for breach thereof.* (Emphasis added.)

Ms Paramjit Kaur for the defendant has raised two arguments in response. Her first is that this is a plain case of frustration. She says that the judge was right in the finding he made upon all the issues. Her second argument is that the decision in *Supamarl* is wholly irrelevant to the present case because of the express clause contained in the second agreement which entitles the defendant to revert to the original position whenever there is a default. Counsel has drawn our attention to the fact that the plaintiff had defaulted in his obligation in June 1991 and for a period of five months thereafter. She says that once the plaintiff defaulted, the relevant clause in the second agreement (to which we have lent emphasis) was activated and her client was accordingly entitled to recover all sums due under the first agreement. Before we address the merits of these arguments, it is necessary for us to examine the relevant principles that govern the issues raised before us.

In *Ramli bin Zakaria & Ors v Government of Malaysia* [1982] 2 MLJ 257 at p 262, Abdul Hamid FJ (later CJ) enunciated what amounts to frustration. He said:

> In short it would appear that where after a contract has been entered into there is a change of circumstances but the changed circumstances do not render a fundamental or radical change in the obligation originally undertaken to make the performance of the contract something radically different from that originally undertaken, the contract does not become impossible and it is not discharged by frustration.

We accept that statement to be an accurate proposition governing the law of frustration. In the words of s 57(2) of the Contracts Act 1950:

> A contract to do an act which, after the contract is made, becomes impossible, or by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.

The element of unlawfulness appearing in the s has no part to play in the present appeal. Here, it is simply a question as to whether the obligation voluntarily undertaken by the defendant became impossible of performance in the sense explained by Abdul Hamid FJ in the passage quoted above.

Mr Ravichandran argues that there is no impossibility involved in the present case because the defendant did not establish that it had done all that it could do to have the order for sale cancelled or withdrawn. In particular,

counsel points out that the defendant could have either appealed to the High Court under s 418 of the National Land Code 1965 against the decision of the land administrator. Or it could have appealed to the then Supreme Court from the decision of the High Court refusing to set aside the order for sale. Neither of these things was done. Counsel also points out that it was open to the defendant to have saved the subject property by participating in the auction under s 265 of the National Land Code 1965. We find much merit in these arguments.

In our judgment, the present case does not concern a supervening event, for there was none. It concerns a change in circumstances that were not radically different from those that prevailed at the time the second agreement was entered into. All that had happened was that the defendant had failed to pursue its best endeavours to secure the sale or withdraw the order for sale. We therefore agree with counsel for plaintiff that the present case is governed by the case of *Dalmia Dairy Industries Ltd v National Bank of Pakistan* [1978] 2 Lloyd's Rep 223 which this court applied in *Dato Yap Peng v Public Bank Bhd* [1997] 3 MLJ 484. We would adopt what Kerr J said in *Dalmia*'s case at p 493:

> However, leaving aside for the moment contracts affected by war, it is settled law in England (and on the evidence also in India) that a supervening prohibition of some contractually undertaken obligation, which can be overcome by obtaining a licence, will only frustrate a contract at once if the person affected by the prohibition can show that no licence could in any event have been obtained. If this is uncertain, then his obligation is to use his best endeavours to obtain the necessary licence, and the contract then only becomes frustrated if and when all such efforts have failed. In such a situation the 'probability test' never appears to have been applied. It is not reflected in *Andrew Millar & Co Ltd v Taylor & Co Ltd* [1916] 1 KB 402 (a case of wartime illegality which was cited by both parties) or in the discussion of that case in *Atlantic Maritime Co Inc v Gibbon* [1953] 2 Lloyd's Rep 294; [1954] 1 QB 88.
>
> However, whatever may be the position in English law, my task is to make a finding on the evidence about the true construction and effect of s 56 in relation to Indian law and what I have called the 'wait and see' and the 'probability' tests. As to these tests I can only find that on the material before me there is no shred of any evidence, other than Mr Lall's unsupported assertion to the contrary, that the 'probability test' is part of the law of India. It is nowhere reflected in the language of s 56, and I do not see how it can be implied. In *Satyabrata*'s case (at p 326) the Supreme Court followed Lord Wright in *Denny Mott & Dickson v James B Fraser* [1944] AC 265 by quoting from his speech at p 274 where he said:
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> > 'The issue (frustration or not) has got to be decided by the court ex post facto on the actual circumstances of the case.'

That brings us to Ms Paramjit's argument that her client was entitled to revert to the original position if there was no frustration. The simple answer to her submission is this.

The primary obligation under the second agreement was on the defendant to do what it promised, namely to have the order for sale cancelled or withdrawn. By June 1991 (date of the alleged default by the

plaintiff) that obligation remained plainly unfulfilled. Since the defendant had breached its part of the bargain it does not lie on its mouth to complain of the plaintiff's default. In our judgment, the plaintiff was clearly within his rights to refuse to continue performance of his obligations under the contract in view of the defendant's default. The clause in the second agreement upon which the defendant relies is accordingly is of no assistance to it.

It follows from what we have said thus far that upon the making of the second agreement and upon the defendant's breach of it, the rights of the parties were to be determined in accordance with that agreement. The defendant in our view did not have the right to have recourse to the first agreement. Accordingly the sums claimed by it in the sessions court action were clearly irrecoverable. However, the plaintiff was under a separate obligation to pay and settle the personal loan given him under the second agreement. Mr Ravichandran accepts that his client is so liable.

For the reasons already given, we are of the view that this appeal must succeed. To summarize, the learned judge was wrong in holding that the second agreement was frustrated. We also hold that the second agreement had been breached by the defendant. We further hold that the first agreement had ceased to be in force. Accordingly we would set aside the orders made by the learned judge. We would enter judgment for plaintiff in his action. We would dismiss the sessions court action. We would uphold the judge's findings in respect of the magistrates court's action. The damages recoverable by the plaintiff must be assessed by the registrar of the High Court. For that purpose, we remit the case to the High Court. In assessing the damages, the registrar must give credit to the defendant for the sums it has recovered in magistrates court action. The plaintiff will have the costs of this appeal as well as the costs in the court below and all costs in the assessment proceedings. The deposit shall be refunded to the appellant.

Appeal allowed.

Reported by Benjamin Yong